

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **201240005**
Release Date: 10/5/2012

Index Number: 6050W.00-00

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

In Re:

Refer Reply To:
CC:PA
PLR-101506-12
Date:
July 09, 2012

Dear :

This is in response to your ruling request submitted by your authorized representative concerning the federal income tax reporting requirements for your wholly-owned subsidiary (Company X) under section 6050W of the Internal Revenue Code (Code) and the regulations thereunder. Specifically, you would like a ruling that Company X:

(i) is not the entity that makes payment in settlement of the reportable transactions described in this ruling request;

(ii) as the tax-reporting designee of a non-U.S. payor that does not have to report payment transactions or obtain additional documentation because its payees are foreign persons (they do not have a U.S. address and as to whom the non-U.S. payor does not know nor has reason to know is a U.S. person), Company X does not have to report such payment transactions;

(iii) as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, Company X may rely on such non-U.S. payor's determination in (ii) that a payee is a foreign person and therefore no information return need be filed with respect to that payee and no additional documentation need be collected as to the payee's foreign status;

(iv) as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, Company X does not have the obligation under the Code or the regulations to obtain documentation to prove foreign person status in the event a payee has a U.S. address or the entity has reason to know that a payee is a U.S. person;

(v) as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, Company X may rely on documentation collected by the entity to

prove foreign person status in the event a payee has a U.S. address or the non-U.S. payor has reason to know that a payee is a U.S. person;

(vi) as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, Company X may collect documentation to prove foreign person status of a payee and the non-U.S. payor may rely on such documentation;

(vii) as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, Company X would not be liable for any penalties for failure to report or inaccurately reporting because the non-U.S. payor did not possess the appropriate documentation even though Company X prepares and submits the information returns.

FACTS:

Company X is a provider of _____ services for consumers, merchants, financial institutions, government agencies, and multi-national corporations located in the United States and internationally. Company X acts as _____ between, for example, merchants and card issuers, settling purchases made by consumers with a credit card. Company X operates in two business segments: North America and International. Company X is incorporated in the United States.

Payment Networks

Many credit cards are processed through one of the major payment networks, such as _____ and _____. These major payment networks have certain prerequisites an entity must satisfy in order to be able to access the payment network and process credit card transactions connected to the payment network's credit cards. Generally, an entity must either (i) be a member of the applicable payment network or (ii) it must have an agreement with a member of the payment network ("Sponsorship Bank").

In addition to membership to the payment network, an entity seeking to provide processing services must have a bank identification number ("BIN"). The BIN is assigned by the payment network in order to identify members and allow accurate identification and routing of the applicable transactions for credit approval. In _____, entities that are not a member of a payment network or members that are not financial institutions must have a contract with a _____ financial institution that is a member of the applicable payment network and has the requisite BINs (BIN banks). Since it is

not a financial institution, Company X has contracts with BIN banks to allow Company X to route transactions to the payment network systems.

In order to initiate the actual transfer of funds to merchants in _____, Company X has established depository and clearing relationships with _____ financial institutions. Company X's two primary depository and clearing relationships are with (1) the _____ and (2) the _____ ; _____ and _____ will be referred to in this ruling request as Settlement Banks. The depository and clearing relationships with the Settlement Banks allow Company X to ultimately clear and settle card transactions with merchants that have been routed through the payment networks via the BIN banks for funding approval

The parties to the agreements with Company X's merchants ("_____ Agreement") vary depending on the payment network. For _____ payment transactions, the _____ Agreement consists of three parties: (1) the merchant, (2) Company X, and (3) the Settlement Bank. In these agreements, both Company X and the Settlement Bank have a contractual obligation to pay the merchant in settlement of its credit card transactions. For _____ payment transactions, the _____ Agreement consists of two parties: (1) the merchant and (2) Company X. In these agreements, Company X has the contractual obligation to pay the merchant in settlement of its credit card transactions.

Company X's agreement with the Settlement Banks makes clear that Company X is designated to undertake all reporting, audit, compliance and related procedures, including the reporting of funding related to the settlement of all payment network credit card transactions that Company X processes.

Company X's Role in Card Transactions

Company X is the _____ between merchants, the payment networks, and the Settlement Banks. When a merchant accepts a credit card as payment, Company X captures the card and transaction information and routes it to the appropriate payment network. The payment network forwards the payment authorization request to the card issuer. The card issuer makes a determination on whether to authorize payment for the transaction based on the cardholder's account information and relays that response to the merchant's terminal via the same communication network.

If payment has been authorized, Company X sends instructions to the appropriate payment network. The payment network transfers the transaction information to the card issuer. The card issuer will then send the appropriate funds through the payment network to the Settlement Bank. Company X then creates a merchant funding file for the Settlement Bank and submits it to the Settlement Bank. The Settlement Bank then submits the merchant funding file to initiate payment to the merchant. Ultimately, the merchant's designated bank account is funded the appropriate amount.

LAW AND ANALYSIS

Section 6050W and Payment Card Transactions

Section 6050W of the Code, as enacted by the Housing Assistance Tax Act of 2008, requires payment settlement entities to file an information return for each calendar year with respect to payments made in settlement of reportable payment transactions with participating payees. Treas. Reg. § 1.6050W-1(a)(3). Section 6050W covers two types of transactions: (1) payment card transactions and (2) third party network transactions. A payment card transaction is any transaction in which a payment card is accepted as payment by a participating payee. Treas. Reg. § 1.6050W-1(b)(1).

A payment settlement entity in the payment card context is a merchant acquiring entity. Treas. Reg. § 1.6050W-1(b)(2). The Code and regulations define a merchant acquiring entity as the bank or other organization with the contractual obligation to make payments to participating payees in payment card transactions. *Id.* If there is more than one entity that qualifies as a payment settlement entity—because more than one entity has the contractual obligation to make payments in settlement of payment card transactions—then only the payment settlement entity that in fact makes payment in settlement of the reportable payment transaction has the obligation to report. Treas. Reg. § 1.6050W-1(a)(4)(ii). The regulations state that a payment settlement entity makes a payment in settlement of a reportable payment transaction “if the payment settlement entity (or electronic payment facilitator) submits the instruction to transfer funds to the account of the participating payee.” Treas. Reg. § 1.6050W-1(a)(2).

Section 6050W puts forth a special rule in the event an electronic payment facilitator (EPF) makes payments in settlement of reportable payment transactions on behalf of the payment settlement entity. I.R.C. § 6050W(b)(4)(B). In that scenario, the Code and the regulations make clear that the EPF must report in lieu of the payment settlement entity. The EPF need not have any agreement or arrangement with the participating payee nor does payment have to come from the EPF's account. Importantly, the EPF is liable for any penalties for failing to comply with section 6050W reporting.

The transactions described above are payment card transactions that are subject to reporting under section 6050W: the merchants with whom Company X has

Agreements accept credit cards as payments for their transactions with consumers. Company X's designation under the regulations varies based on the parties to the Agreement.

In agreements where both Company X and a Settlement Bank are parties to the agreement with the merchant, both Company X and the Settlement Bank satisfy the definition of merchant acquiring entity, which is the payment settlement entity for purposes of payment card transactions. I.R.C. § 6050W(b)(1); Treas. Reg. § 1.6050W-1(b)(2). As discussed, if there are multiple entities that qualify as payment settlement entities with respect to a reportable payment transaction, then the payment settlement entity that in fact makes payment in settlement of the reportable payment transaction—defined as submitting the instructions to transfer funds to the account of the participating payee—is obligated to report under section 6050W. Treas. Reg. § 1.6050W-1(a)(4)(ii); Treas. Reg. § 1.6050W-1(a)(2). The Settlement Bank is the entity that submits the instructions to initiate payment to the merchant.

In agreements where Company X is the only party with a contractual obligation to pay the merchant, Company X is the exclusive merchant acquiring entity and the payment settlement entity for those transactions. In these cases, however, Company X contracts with a Settlement Bank to make payments in settlement of the reportable payment transactions on behalf of Company X. As discussed above, the card issuer will send the appropriate funds to the Settlement Bank. Company X will then prepare the merchant funding file for the Settlement Bank. The Settlement Bank, acting as an electronic payment facilitator, is the entity that submits the instructions to transfer payment to the merchant. Treas. Reg. § 1.6050W-1(d)(2); Treas. Reg. § 1.6050W-1(e), Example 22.

Foreign Address and Designation Rules

Another relevant factor for determining the existence of a reporting obligation is the status of the payee. The Code makes clear that reporting is necessary for reportable payments made to a participating payee. I.R.C. § 6050W(a). Section 6050W(d)(1)(B) provides that, except as provided in regulations or other guidance, the term participating payee does not include any person with a foreign address. The regulations provide two separate rules for determining whether a person has a foreign address, depending on whether the payor is a U.S. payor or a non-U.S. payor. The regulations impose documentation requirements on payors in instances where there is doubt as to whether a payee has a foreign address and is therefore a foreign person not subject to reporting. After publication of the regulations, the Internal Revenue Service ("Service") published Notice 2011-71, which provides interim guidance relating to the rules U.S. and non-U.S. payors need to follow when determining whether a person has a foreign address. Notice 2011-71, 2011-2 C.B. 233. The primary purpose of Notice 2011-71 was to relax the documentation requirements for U.S. payors in certain contexts.

Under the regulations, a non-U.S. payor does not have to report payment transactions to a payee that does not have a U.S. address as long as the non-U.S. payor neither knows nor has reason to know that the payee is a U.S. person. If a payee does have a U.S. address, the non-U.S. payor may treat the payee as a foreign person if it obtains the documentation requirements put forth in Treas. Reg. § 1.1441-1(e)(1)(ii). Treas. Reg. § 1.6050W-1(a)(5)(ii)(B).

In light of the changes put forth under Notice 2011-71, a U.S. payor needs to report payment transactions made outside the U.S. to an offshore account only if: (i) there is a U.S. address associated with the participating payee (whether a residence address or correspondence address); (ii) the payment settlement entity has standing instructions to direct the payment to a bank account maintained in the United States; (iii) the participating payee submits for payment in U.S. dollars; or (iv) the payment settlement entity knows or has reason to know that the participating payee is a U.S. person. If any of the first three criteria are present, the U.S. payor may still show that a payee is a foreign person by obtaining the documentation put forth in Notice 2011-71.

The regulations also provide a transition rule for contracts entered into before January 1, 2011. A payment settlement entity that is a U.S. payor is not required to report payments made to a participating payee with a foreign address as long as the U.S. payor neither knows nor has reason to know that the payee is a U.S. person, effectively applying the same reporting standards applicable to non-U.S. payors. For this purpose, a renewal of such a contractual obligation will not result in a new contractual obligation unless there is a material modification of the contractual obligation.

Despite being a payment settlement entity or electronic payment facilitator under the Code and regulations, the regulations allow for such parties to designate, by written agreement, any other person to satisfy the reporting requirements of section 6050W. Treas. Reg. § 1.6050W-1(d)(3). Designation, however, does not relieve the party with the reporting obligation from penalties for failing to comply with section 6050W. *Id.*

The ruling request states that Company X is a U.S. payor and that the Settlement Banks are non-U.S. payors. Accordingly, the Settlement Banks do not have to report—under the non-U.S. payor rules—payment transactions for merchants that do not have a U.S. address and for which the Settlement Banks neither know nor have reason to know that the merchant is a U.S. person. As the Settlement Banks' (non-U.S. payor) designee, Company X may rely on Settlement Banks' determination that a merchant is a foreign payee. See Treas. Reg. § 1.6050W-1(d)(3).

Additionally, because Company X is merely the designee and not the entity with the section 6050W reporting obligation under the Code, Company X does not have an obligation under section 6050W to obtain documentation necessary to establish that a payee is a foreign person.

Because Company X is merely the designee and not the entity with the section 6050W reporting obligation under the Code, Company X also may rely on documentation collected by Settlement Bank for purposes of establishing that a payee is a foreign person because the Settlement Bank has the section 6050W reporting obligation.

Company X may collect documentation to establish that a payee is a foreign person and Settlement Bank may rely on such documentation. That reliance, however, does not relieve the Settlement Bank from any liability for reporting failures. Treas. Reg. § 1.6050W-1(d)(3).

Company X, as the designee for section 6050W reporting is not liable for any penalties for failing to report or inaccurately reporting because the Settlement Bank did not possess the appropriate documentation. As discussed above, a designation does not relieve the party with the reporting obligation from liability for any reporting failures. Treas. Reg. § 1.6050W-1(d)(3); Treas. Reg. § 1.6050W-1(e), Example 22.

CONCLUSION

- (i) Company X is not the entity that makes payment in settlement of the reportable transactions described in this ruling request and therefore does not have a section 6050W reporting obligation;
- (ii) Company X, as the tax-reporting designee of a non-U.S. payor that does not have to report certain payment transactions nor obtain documentation as to the foreign person status of certain payees, does not have to report such payment transactions;
- (iii) Company X, as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, may rely on such non-U.S. payor's determination that a payee is a foreign person when determining whether an information return needs be filed with respect to that payee;
- (iv) Company X, as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, does not have the obligation under the Code or the regulations to obtain documentation to prove foreign person status in the event a payee has a U.S. address or the non-U.S. payor has reason to know that a payee is a U.S. person;
- (v) Company X, in its role as the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, may rely on documentation collected by the non-U.S. payor to prove foreign person status in the event a payee has a U.S. address or the U.S. payor has reason to know that a payee is a U.S. person;
- (vi) Company X, in its role as a the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, may collect documentation to prove

foreign person status of a payee and the non-U.S. payor may rely on such documentation but the non-U.S. payor is still liable for any reporting failures;

(vii) Company X, in its role as a the tax-reporting designee for a non-U.S. payor with a potential section 6050W reporting obligation, would not be liable for any penalties for failure to report or inaccurately reporting because the non-U.S. payor did not possess the appropriate documentation even though Company X prepares and submits the information returns.

These conclusions are based exclusively on the information provided and the representations made by the requestor. This letter ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Charles A. Hall
Senior Technician Reviewer, Branch 1
(Procedure & Administration)

cc: